

Internal Revenue Service
memorandum

CC:TL-N-9437-90
TS/P/MAKEYES/alb

date: NOV 1 1990

to: District Counsel, Manhattan NA:MAN
Attn: Michael Wilder

from: Acting Chief, Tax Shelter/Partnership Branch CC:TL:TS/P

subject: [REDACTED] Piggyback Agreements
TL-N-9437-90
CC:TL:TS/P Keyes Wilson

This memorandum is in response to your request for technical advice on the above-entitled cases.

ISSUES

1. What are the consequences of the 5th Circuit's opinion in [REDACTED], dated [REDACTED], on the Tax Court's opinion in [REDACTED]?

(a) What are the consequences of the 5th Circuit's opinion on the [REDACTED] case which is piggybacked to [REDACTED] for the underlying adjustment, but which was tried on the negligence issue?

2. What are the consequences of the 5th Circuit's opinion on the piggyback agreements for docketed and nondocketed cases?

CONCLUSION

We agree with the well written positions you assert in your incoming request on the effect of the [REDACTED] appellate opinion on the [REDACTED] case, as well as on the other piggybacked cases. It will be necessary to have the court rule on at risk in the [REDACTED] case since the piggyback agreements are probably unenforceable in light of the Court of Appeal's opinion in [REDACTED] that at risk was not an appealable issue under the circumstances. We also agree that the Tax Court's opinion in [REDACTED] will not have a collateral estoppel effect on [REDACTED]'s later years. We recommend that since the 5th Circuit dismissed the [REDACTED]'s appeal on the at risk issue on the ground that it was not applicable to the deficiency at issue, the [REDACTED] brief be supplemented to address the at risk arguments. The other investors can then be piggybacked to [REDACTED] to resolve the at risk issue.

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FACTS

The [REDACTED] case involved the [REDACTED] and the purchase and leaseback of [REDACTED] equipment. [REDACTED] was the controlling case to which all other investors in [REDACTED] were piggybacked for the adjustments made relating to the Trust and the [REDACTED] leasing activities. In addition, some investors are piggybacked to the [REDACTED] case solely for the negligence issue.

[REDACTED] is piggybacked to [REDACTED] for the underlying adjustments for [REDACTED], but was tried on the negligence issue. In [REDACTED], the record of [REDACTED] was stipulated to, including the ultimate findings. Only additional facts necessary for the negligence issue were presented at the [REDACTED] trial. The opening briefs for [REDACTED] were filed prior to the 5th Circuit's opinion in [REDACTED]. Reply briefs for [REDACTED] were due [REDACTED].^{1/} The Court has specifically asked the parties to consider the effect of [REDACTED] on the [REDACTED] case.^{2/}

In [REDACTED], the Tax Court rejected respondent's arguments that the losses were based upon sham transactions, that taxpayers had not obtained the burdens & benefits of ownership, and that they lacked a profit motive. Although the Court held that the losses from the [REDACTED] could not be entirely disallowed, it did find that the losses were limited by the at risk rules. In reaching that conclusion, the court found the Trust Note for the purchase of [REDACTED] equipment protected the investors from loss, and was not recourse. Therefore, losses were limited because the investor was not at risk with respect to the note issued by the partnership for the purchase of [REDACTED] equipment. In addition, the Court found that section 6661 and 6621(c), as well as section 6653 were applicable.

^{1/} Our recommendation regarding the advice requested was discussed with your office prior to the due date of the reply briefs in [REDACTED]. Your office was attempting to arrange a conference call with the parties regarding the filing of briefs on the at risk issue.

^{2/} Taxpayers are arguing that they want a new test case for the section 465 issue, including a new trial. They stated that they may possibly try a later year for [REDACTED]. At the very least, they want to submit briefs on the at risk issue in the [REDACTED] case.

Petitioners' appealed the section 465 issue, as well as the additions to tax. In [REDACTED], the 5th Circuit dismissed the petitioners' appeal and held that it could not consider the merits of it because the at risk issue was not necessary to support the Tax Court's deficiency judgment which arose solely from an improper claim of investment tax credit. The Circuit Court also remanded the case back to Tax Court to determine if the additions to tax were applicable in light of its opinion that section 465 was irrelevant to the Tax Court's decision.

Because the Fifth Circuit did not address the merits of the appeal of the at risk issue, the question arises as to how the Tax Court's finding on section 465 applies to these other investors, and even the later years of [REDACTED], where the taxpayers are clearly not at risk because of insufficient cash investment.

DISCUSSION

We agree with your conclusion that the 5th Circuit's dismissal of the appeal of the section 465 issue in [REDACTED] has the effect of preventing the application of collateral estoppel with respect to [REDACTED]'s later years. In addition, it probably makes the piggyback agreements for [REDACTED] and the other investors unenforceable. Although the underlying theory behind piggyback agreements is not collateral estoppel, but rather, contract theory, the end result is the same for these cases. Collateral estoppel would not apply to [REDACTED]'s later years because the Tax Court's deficiency decision in [REDACTED] was not based upon the at risk issue. The piggyback agreements would be unenforceable because the section 465 issue is not addressed with finality because of the Fifth Circuit's refusal to review the issue on appeal.

Because the appellate court found that the at risk issue was not part of the underlying Tax Court deficiency judgment, it could not consider the merits of the appeal on that issue. The Fifth Circuit cited W. W. Windle v. Commissioner, 550 F.2d 43, 45-46 (1st Cir. 1977), cert denied, 431 U.S. 966 (1977) for that proposition. In Windle, supra, at 46, the First Circuit found that the doctrine of collateral estoppel may be invoked only to questions of law and facts essential to a judgment. If the contested finding is immaterial to the Tax Court's decision it would be without collateral estoppel effect. In [REDACTED], the 5th Circuit refused to address section 465 since it was immaterial to the Tax Court's decision. Consequently, the Tax Court's opinion regarding section 465 will not collaterally estop [REDACTED] from contesting the section 465 issue in later years.

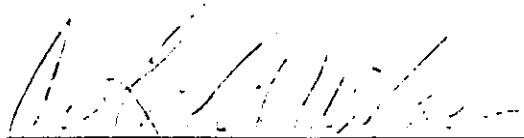
In piggyback agreements, taxpayers and the Commissioner agree to bind themselves to the results of a particular case. In binding themselves to a particular case they mutually agree to a vehicle that will resolve the underlying issues with finality. This includes appellate review since the piggyback agreement specifically references a final decision under section 7481. In these cases, section 465 is an issue that the parties intended to be determined with finality.

In light of the fact that the only theory the Tax Court found applicable to the [REDACTED] project was our at risk argument, (despite the fact that for [REDACTED] [REDACTED] did have sufficient cash investment to be at risk for that year), it is imperative that the at risk argument be validly before the court. Because of the 5th Circuit's opinion in [REDACTED], we recommend arguing section 465 in the [REDACTED] briefs. If possible, request leave from the Court to file supplemental briefs on the section 465 issue. By filing supplemental briefs a response to any arguments raised by either party can be addressed. In addition, we recommend getting new piggyback agreements, with [REDACTED] as the controlling case.

Whether a new trial is warranted is really a decision your office should more appropriately decide. If the facts presented in [REDACTED] are sufficient for the section 465 argument then obviously your office should oppose any new trial, or further testimony and instead push for arguments in the brief.

In light of this we would recommend that the piggybacked cases be bound to [REDACTED] for the section 465 issue and the new piggyback agreements would need to specify that these piggyback agreements are controlling.

Should you have any additional questions please contact Marsha Keyes at FTS 566-4174.



CURTIS G. WILSON